

“GOING WITH THE FRANCHISING FLOW”

**An exploration of partnerships
for the operation and maintenance
of water services infrastructure**

Kevin Wall & Oliver Ive

**“Going with the franchising flow”:
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operation and maintenance of water
services infrastructure**

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Water Research Commission

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- Going with the franchise flow: An exploration of franchising partnerships for the operation and maintenance of water services infrastructure. **(Report TT 432/1/10)**
- Water services franchising partnerships: Overview of the concept of franchising and its relevance to water services. **(Report TT 432/2/10)**
- Water services franchising partnerships: Review of policy, regulation and legal aspects. **(Report TT 432/3/10)**
- Water services franchising partnerships: Modelling of selected water services operational elements. **(Report TT 432/4/10)**
- Water services franchising partnerships: Institutional review for the application of franchising. **(Report TT 432/5/10)**
- Water services franchising partnerships: Establishing criteria for the selection of water service franchisors, partnerships and franchisees. **(Report TT 432/6/10)**
- Water services franchising partnerships: Business analysis case study: schools sanitation O&M. **(Report TT 432/7/10)**

Report TT 432/1/10 (*Going with the franchise flow: An exploration of franchising partnerships for the operation and maintenance of water services infrastructure*) is the only one in the series that has been printed. The rest are available on the WRC web site (www.wrc.org.za) from where they can be downloaded.

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Executive summary

How is it that one can go to some parts of our country and buy clean petrol and clean (if, arguably, unrepresentative of good dietary practice) hamburgers, but cannot get clean water from a tap or hygienic and environmentally acceptable sanitation? Especially when the oil from which the petrol is made has to be imported from very far away, whereas the "raw material", so to speak, for the clean water can be sourced from relatively close by.

How can such a thing be?

There are lots of possible reasons for this, two of which are:

- The first one is that the manager or owner of the retail outlet, and also the staff, know that if they cannot reliably, every day, provide those hamburgers or that petrol, they will not get paid. If something goes wrong, they know that they have to get it right – and quickly. That is "incentive".
- The second reason is that the staff of the outlet, and all the people responsible for producing the product to be sold (e.g. those who refine the petrol), making sure that it gets to the outlet, and so on, are properly trained – trained, that is, each to the level required for his or her job, BUT with an obligation (maybe a contract) to call for the higher levels of expertise when these are needed, and a matching obligation to provide that assistance. That is known as "capacity".

The questions that this study addressed are:

- What is it that makes the hamburger outlet or petrol station work as well as it does – what are the operational principles? and
- Can these principles be applied to providing acceptable sanitation and clean water?

Introduction

The rapid rate of construction and commissioning of new water services infrastructure is severely challenging the public sector institutions in South Africa responsible for operating and managing this infrastructure. Innovative approaches are required. But even if all the existing water services institutions were coping with the responsibility, there would be good reason to investigate alternative institutional models on the grounds that it needs to be found out if alternatives:

- could be more cost-effective, and/or
- could allow existing role-players to focus on their other responsibilities, and/or
- could offer a range of other advantages (including greater local economic development).

There is an alternative institutional model that is suited more for the ongoing operation and maintenance of water services systems than for investment in new infrastructure – and, importantly, that is friendly to small business and local economic development. This alternative is the franchising partnership. However there is little experience of this approach having been applied to water services infrastructure operation and maintenance anywhere in the world, although some existing partnerships share some of the characteristics of the franchise approach.

The principles of franchising partnerships in the generic (i.e. not specific to water services or any other sector) sense can be summarised as follows:

- Franchises' success is based on replication of success, efficient logistics and a trained and capacitated workforce.

- Franchisee small businesses are relatively easy to establish.
- Franchising is robust, and able to ensure consistent quality products and services.
- Franchisees are obliged to adopt the tried and tested systems and procedures of the franchisor, and to accept the quality control of the franchisor – resulting in higher quality assurance and greater efficiencies.
- Franchises are able to innovate and develop constantly.

Franchising is a way of accelerating the development of a business, based on tried and tested methodology. The franchise system firstly correlates and systematises the business, and then facilitates the setting up of the business, and supports and disciplines it thereafter.

The key is the incentive, to franchisor and franchisee alike, to improve efficiency, and to provide improved service reliability and quality control.

A Water Research Commission (WRC) scoping study completed in 2005 (Wall, 2005) found that franchising partnerships could alleviate and address many challenges in the management of water services. At the same time, franchising would support the development of local microenterprises and broad-based black economic empowerment (BBBEE), all within the public sector service delivery environment.

The case for water services franchising partnerships

The most comprehensive review to date of the state of infrastructure in South Africa has been that released by the South African Institution of Civil Engineering (SAICE). At the end of 2006 SAICE released the first ever “report card” of the state of South African infrastructure (SAICE, 2006). In respect of the major urban areas, SAICE assigned water infrastructure the grade of “C+” and sanitation “C”, whereas it gave “D-” and “E” (the next-to-the-lowest-possible grade) to the equivalents in small towns and rural areas. SAICE found that, to a very significant extent, the difference lay in infrastructure in the major urban areas being in the care of skilled professionals – and the other areas not having access to these skills levels.

Significant improvements would soon be seen if the generally under-qualified or under-resourced water services staff of the municipalities and other water services authorities (WSAs) outside the major urban areas could enjoy ongoing support, mentoring and quality control – or if the WSAs could enter into partnerships with microenterprises which would, through franchising partnerships, enjoy the necessary ongoing support, mentoring and quality control.

Given that the costs of the franchisor’s higher levels of specialist expertise would be shared by several franchisees, the franchisor could afford to make this expertise available to each of them on an as-needed basis, and could provide other resources normally only available to larger water services providers. This holds significant benefits for WSAs.

The WSA client’s competence to monitor performance and enforce contract compliance is key to it effectively using the microenterprise sector. However if an WSA is short of management resources, it would be putting these to more efficient use if it managed the work of the contractor rather than tried to cope with the operational issues itself.

A few water services franchisors have long been operating in South Africa. They are successful financially and in terms of the service (operation and/or maintenance of an element or elements of the water services delivery chain) that they provide to their current market niche (invariably within the private sector). More than one franchisor would like to extend its services to WSA-owned infrastructure, but they do not find the environment conducive.

The Drain Surgeon is a well-known franchisor based in Gauteng, but with franchisees under the same brand name in all major centres of South Africa. Its business model is undoubtedly very successful, but much of the business information pertaining to its business model, and the business models of other water services franchising companies, is, understandably, guarded by the companies that possess it, and which have, with little if any exception, gained their information the hard way – through experience! It is their competitive advantage, and they are willing to share only up to a point.

Thus a major motivation for the research has been the WRC's wish to extend water services franchising beyond its current niches, and to explore and pilot franchising application across operation and maintenance of a range of public sector water services infrastructure elements; further, to place in the public domain the business information (e.g. methods, financial viability) that it (the WRC) develops.

Franchising partnerships design

The WRC has been researching a partnership concept, making use of the principles of franchising, for improved water services infrastructure operation and maintenance. In this concept, ownership of the water services infrastructure remains with the public sector (e.g. the WSA).

The concept has been formulated with a view to improving water services operational quality and efficiency through introducing a new (to water services) supply-side operation and maintenance provider mechanism.

Many South African WSAs do not have staff or systems to deliver a reasonable service. A carefully designed set of WSA/franchisor/franchisee arrangements, efficiently implemented, could assist. At the same time, franchising offers opportunities to the microenterprise sector and to local economic development. Franchisees are microenterprises, but their association with a franchisor gives them considerable advantages – reflected in the better service that they can provide – over stand-alone microenterprises.

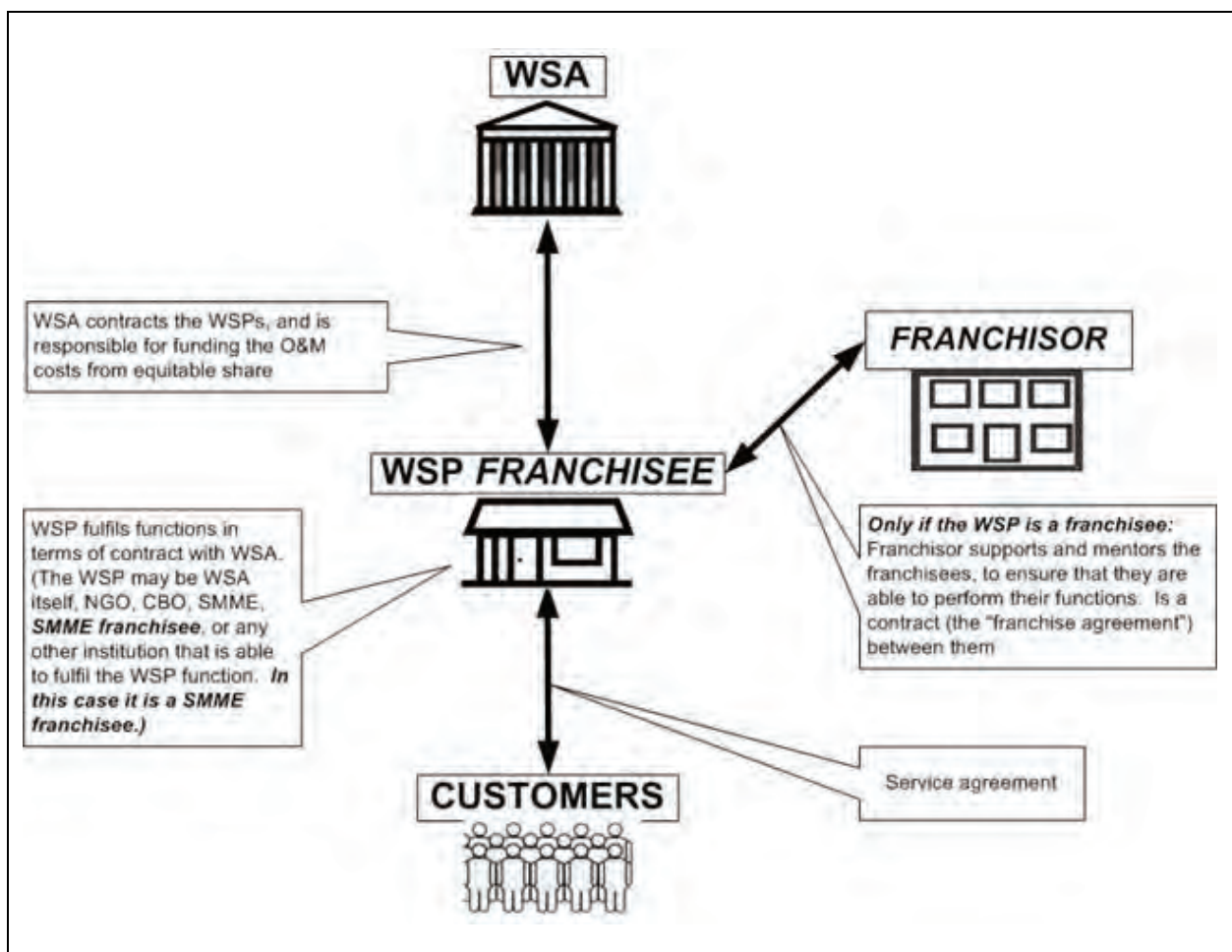
Franchising might not be ideal, but it might in many situations offer the prospect of improved operation and maintenance of water services. However three main priorities need to be addressed simultaneously if the operation and maintenance of public sector water services infrastructure is, in the cause of improved water services provision, and to the benefit of water services users, to be franchised where it is appropriate to do so. A “three-step breakthrough” is needed:

- The first step is the breakthrough to acceptance by WSAs of outsourcing the operation and maintenance of infrastructure that they, the WSAs, own. (To emphasise: this outsourcing need not necessarily be to the private sector – it could also be to NGOs and CBOs.)
- The second is the acceptance that the institutions outsourced to could be microenterprises.
- The third step is the acceptance that these microenterprises could be franchisees. (This third step should not be a problem once the second level is in place. Franchised microenterprises should be a concept considerably easier to convince clients of the merits of than the idea of microenterprises that are stand-alone.)

Note that what is good or bad for microenterprises is good or bad for franchising partnerships. But the converse doesn't necessarily apply – or, putting it another way, a franchisee microenterprise, given the support it would receive from the franchisor, would in all likelihood find it easier to meet some regulatory and other requirements than would a stand-alone microenterprise, everything else being equal.

Finally, whereas a business based on a single element of the water services delivery value chain might not be viable, a franchisee might be able to make a viable business by offering several water-related services, thereby achieving dual objectives, viz.:

The figure below depicts a possible set of contractual relationships.



This figure has been kept as simple as possible, so as to not obscure the principal relationships, but in practice it is unlikely that any microenterprises would be water services providers (WSPs) directly contracted to WSAs. Their small size counts against them. In nearly all conceivable circumstances, the WSA will contract with one or a small number of "prime contractor"-WSPs in its area, and these will in turn contract with smaller "subcontractor" WSPs, including the likes of CBOs and microenterprises (which might or might not be franchisees).

Whereas a WSA may require contractual recourse not only to the franchisee, but also to the franchisor, the franchisor could be a co-signatory to the contract or a guarantor of the performance of the franchisee. This would, if it were deemed to be necessary, require an additional contract – one that closes the loop between the franchisor and the WSA. The WSA may require this contractual assurance that the franchisee will be supported by strong management, and also that the franchisor is able to make alternative arrangements which will ensure continuity of service should the franchisee for any reason whatsoever fail to meet its contractual obligations to the WSA. Especially this assurance could be necessary if the franchisor's expertise or track-record is a significant reason for contracting with the franchisee, and the franchisee is a largely unknown quantity.

Franchising partnerships potential

The concept addresses the lack of higher-level expertise that has so often been identified as a key to improvement of service, especially in the more remote areas. The local staff can deal with day-to-day operational needs, but are not able to deal with anything more demanding than that. The essence of water services franchising partnerships is the creation of a pool of appropriate expertise upon which the local operators can draw, a restructuring of the local responsibility for operating, and the creation of a two-way obligation – an obligation to call for assistance from the pool, and an obligation to respond rapidly to that call. All of this together with the incentive structures to ensure that it happens.

In brief:

- On most days at the (for example) treatment works, nothing out-of-the-ordinary happens. Franchisee staff, who are appropriately skilled, are able to cope.
- When major maintenance or upgrading is needed, or when there is a breakdown, those staff know who to call at the franchisor in order to bring the higher level of skill.
- And they know that the people they call WILL help, because there is a binding contract and a shared reputation.
- It is two-way obligation – an obligation on the franchisee to ask for help, and an obligation on the franchisor to give the help.
- Cost of the higher skills levels, which are needed only intermittently, is spread across many sites – thus cost per site is low.

The franchisees would be microenterprises and CBOs. The franchisors would be any institution that has the required expertise, is willing to provide the service, and would not be in a conflict of interest were they to offer to provide the service.

There are already many potential sites for water services franchising partnerships, in the sense that much water services infrastructure is already in place but is not being operated and maintained properly at the present time.

Other water services operation and maintenance tasks with apparent potential for franchising include (but are not limited to) leak detection, borehole management, management of municipal treatment works, management of treatment package plants, meter reading, pit-emptying services, laboratory services, data management, demand and pressure control management, and site and property management. The WRC has modelled some of these.

In setting up a franchisor-franchisee partnership, the sequence of events will probably be that it will initially only be entities (companies or large NGOs) that see themselves as potential franchisors that will have the capacity to initiate water services franchising partnerships proposals. They will select water services elements and will formulate the business models to go with each. They will then look for sites to apply the models, and will seek the cooperation of the WSAs or other infrastructure owners. Finally they will offer the business to potential franchisees, or will attempt to nurture potential franchisees.

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Notes

The report is written primarily for a fairly senior level of readership – say senior government official, municipal manager, or senior staff of potential franchisor.

Words or passages enclosed by square brackets [], within quotations from other texts, are the current authors' interpolations.

All references to or quotations from policy, statutes, regulations and so forth are to the best understanding of the authors up to date to August 2007. Developments (if any) since that time have not been captured.

Throughout the text "the research" or "the study" refers to WRC Research Project K5/1610, the "Water Services Franchising Partnerships" project.

Note that whereas all WSAs are municipalities or groups of municipalities, not all municipalities are WSAs. Nonetheless, in this document the terms "WSA" and "municipality" are used interchangeably unless only one of "WSA" or "municipality" is intended, in which case this is clearly indicated.

Similarly, in this document the terms "customer" and "end user" are used interchangeably unless only one or the other is particularly intended – which instances are also clearly indicated.

Abbreviations and acronyms

BBBEE	Broad-Based Black Economic Empowerment
BEE	Black Economic Empowerment
CBO	Community-based organisation
CIDB	Construction Industry Development Board
CSIR	Council for Scientific and Industrial Research
DPLG	Department of Provincial and Local Government
DWAF	Department of Water Affairs and Forestry
FASA	Franchise Association of Southern Africa
MFMA	Local Government Municipal Finance Management Act
MSP	Municipal Services Partnerships
NGO	Non-governmental organisation
SAICE	South African Institution of Civil Engineering
SALGA	South African Local Government Association
SMME	Small, medium and micro enterprises
WRC	Water Research Commission
WSA	Water services authority
WSP	Water services provider

Definitions

Frequent reference is made in literature to “**community-based**” or organisations that are “based in the community”. It is often not clear if it is intended that these terms exclusively refer to non-profit organisations or could include profit-seeking organisations. Is the intention of referring to an organisation as “based in the community” to indicate that it is geographically located in the community that it serves and draws most if not all of its personnel (whether they be volunteers or paid) from that same community? The South African Local Government Association (SALGA) has made its interpretation clear. A “community-based organisation (CBO)” is “a not-for-profit organisation within a specific community, with community representatives, that provides a service to that community with the community's mandate or is representing the overall interests of the community.” (SALGA 2005, page 3)

For the purposes of the current document, the term “small, medium or micro enterprise”, or SMME, indicates a profit-seeking organisation, that might or might not be based in a community, drawing personnel from that community, and serving that community. Usage in the current document of “community-based organisation”, abbreviated CBO, is less rigid, but is generally intended to indicate a non-profit organisation. If however the reference to CBOs is a quotation or a paraphrasing from another document, then the meaning intended by the authors of that document is that which rules.

“**Delivery**” embraces not just the placing in service of infrastructure, but the appropriate operation, including maintenance, of that infrastructure for the whole of its designed life.

“**Maintenance**” is in the current document used as a generic term to include repair of infrastructure, refurbishment and renewal, and provision for replacement of that infrastructure.

- “**Water services**” means water supply services and sanitation services.
- “**Water services authority**” means any municipality, including a district or rural council as defined in the Local Government Transition Act (South Africa 1993), responsible for ensuring access to water services.
- “**Water services institution**” means a water services authority, a water services provider, a water board and a water services committee. This institution can be a statutory authority, private company, group of individuals, or an individual, or any combination of these.
- “**Water services provider**” means any person who provides water services to consumers or to another water services institution, but does not include any person who is obliged to provide water services to another in terms of a contract where the obligation to provide water services is incidental to the main object of that contract.

1. Introduction

The WRC has since 2002 undertaken pioneering research into and development of water services franchising partnerships in South Africa, exploring the concept of franchising and its relevance to the water services delivery process.

There is a need for institutional innovations aimed at increasing the coverage and reliability of public sector (and in particular municipal) water services, and sustaining those services. The research into an alternative service delivery institutional concept, *viz.* franchising partnerships for the operation and maintenance of water services, is novel, as it explores an institutional model aimed at relieving or filling the capacity gap from which many municipalities suffer.

South Africa and local government, assisted by the national Department of Water Affairs and Forestry (DWAF) and other role-players, has in the past dozen years been remarkably successful in answering the challenge of services provision. Large numbers of households are now supplied with water services of a wide variety, thanks to massive investments in infrastructure and institutional development. Although there are many who are still not able to access services, this achievement is exemplary.

However, this very success is creating problems now, and for the future. As the number and complexity of water services systems increases, so the operations and maintenance workload escalates. The rising challenge is to ensure that local government water services provider (WSP) organisations can manage all the new systems sustainably.

Conventional wisdom, supported by research, indicates that the capacity of many local governments in South Africa to adequately provide even basic levels of water services to all their citizens on a sustainable basis is in question. The challenge of exploring a range of options to support these organisations also represents an opportunity to selectively incubate innovations on an experimental basis, following a tradition of South African leadership in public sector-driven partnerships with the private sector.

There is a need to make use of the potential of small, medium and microenterprises (SMMEs) to assist public sector water services providers. However the barriers to entry for the smaller or start-up company are substantial. But if these could be overcome – and franchising is one way to mitigate them – then there would likely be many opportunities for local economic development. The twin driving forces of the franchising partnership concept are the profit motive and the existence of a successful business model that can be copied widely – neither of these is currently in evidence in the water services sector.

DWAF and others have for a number of years considered that the potential for franchising in the water services sector ought to be investigated. For various reasons this has never been done.

The first study of water services franchising partnerships commissioned by the WRC indicated that there are opportunities in the water services delivery chain, and recommended that these be explored. (Wall, 2005)

The objective of a second study commissioned by the WRC, and now completed, was to identify the scope for franchising partnerships for the operation and maintenance of selected water services infrastructure, to establish the viability of franchising partnerships, and to make a case for outsourcing to franchises to be considered by water services institutions.

This study further established the value and feasibility of water services franchising partnerships, specifically with respect to the operation and maintenance of water services infrastructure. The study:

- Further explored the concept of franchising partnerships and its relevance to the water services delivery chain.
- Identified and determined those elements in the water services delivery chain which offer the greatest scope for franchising partnerships.
- Undertook a review of the policy, legal, financial, regulatory and procurement issues which impact on the concepts of franchising partnerships.
- Identified those elements in the water services delivery chain which offer the greatest scope for franchising partnerships for the operation and maintenance of that infrastructure.
- Developed business analyses (i.e. models) for the areas identified by the research, with consideration for the legal, regulatory etc. aspects.
- Conducted a case study of an element in a hypothetical situation, to see how the business model would work.

The anticipated longer term outcome, when franchising partnership models have been widely introduced, is that there will in a significant number of instances be reliable water services delivery where this is not the case at present. In addition:

- for water services institutions, an alternative, and in many circumstances superior, delivery concept will be available;
- employment opportunities will be created by small-scale services providers; and
- for potential entrepreneurs, and for broad-based black economic empowerment (BBBEE), new business opportunities will be made accessible and viable.

2. The case for water services franchising

The rapid rate of construction and commissioning of new water services infrastructure is severely challenging the institutions responsible for operating and managing this infrastructure. Innovative approaches to water service delivery are required. But even if all the existing institutions were coping with the water services delivery responsibility, there would be good reason to investigate alternative institutional models, on the grounds that it needs to be found out if alternatives:

- could be more cost-effective, and/or
- could allow existing role-players to focus on their other responsibilities, and/or
- could offer a range of other advantages (including greater local economic development).

There is an alternative service delivery institutional model that is suited more for the ongoing operation and maintenance of water services systems than for investment in new infrastructure – and, importantly, that is friendly to small business and local economic development. This alternative is the franchising of water services. However there is little experience of this approach anywhere in the world, although some existing partnerships share some of the characteristics of the franchise approach.

The barriers to entry for the smaller or start-up company are substantial. But if these could be overcome – and franchising is a way to overcome them – then there will be many opportunities for improved water services and for local economic development. The twin driving forces of the franchising concept are the existence of a successful business model that can be copied widely (there have up to now been very few such models for the water sector) and the profit motive.

Franchising is a way of accelerating the development of a business, based on tried and tested methodology. The franchise system firstly correlates and systematises the business, and then facilitates the setting up of the business, and supports and disciplines it thereafter. Franchising allows small-scale service providers to become formalised and to be supported by a better resourced franchisor, giving them access when they need it to the higher levels of expertise that they do not require – and could not afford to have – on a daily basis.

Early in the research, it became clear that the greatest opportunity for franchising partnerships to add value could be found in operation and maintenance of water services infrastructure. Thus the focus has been in respect of operation and maintenance. The key to improving operation and maintenance of water services infrastructure through franchising partnerships is the incentive, to franchisor and franchisee alike, to improve efficiency, and to provide improved service reliability and quality control.

The WRC has explored the concept of franchising, its relevance to the water services sector, and its prospects as an institutional option for water services operations and management. The research has found that the franchising partnership concept, applied to water services delivery, could in favourable circumstances both alleviate problems encountered in, and raise the efficiency of, water services delivery. At the same time, franchising would stimulate small business activities.

These studies have, further, described at a conceptual level how a water services franchise model could be made available to emerging entrepreneurs, and have concluded that franchising water services could be the basis of a viable business. The franchise would be in respect of a component of the value chain that is suitable for small business because it can be readily systematised.

The WRC finds an indisputable need for alternative water services provider systems, and for local economic development, and that there is potential through water services franchising to simultaneously:

- more consistently deliver water services to specification;
- improve water services efficiency; and
- promote local economic development, SMME development (especially at the microenterprise scale) and broad-based black economic empowerment (BBBEE).

The WRC study (Wall, 2005) found that it is essential to the success of water services franchising partnerships that, *inter alia*:

- Service to customers meets the specification in the franchise contract with the water services authority
- Suitable franchisors are willing and available
- Local entrepreneurs are willing to take up water services franchise opportunities
- Franchising proves to be a viable business for franchisor and franchisee alike
- Funding partners support water services franchising partnerships in just the same way as, in comparable circumstances, they support water services provision by other institutional means

On the last of these points: Franchising must benefit from the funding streams (e.g. the Equitable Share Programme) to the municipality to the same extent as these streams are intended to benefit any other type of water services provider, including the municipality itself.

Franchisee water service providers, dependent for their livelihood on the success of their business, would have a strong incentive to perform, and would also enjoy the benefit of the franchisor's expert guidance and quality assurance.

This help from the franchisor would be of particular value in WSAs away from the major urban centres, few of which can afford to employ competent qualified staff beyond basic skills levels. As an illustration of the direct effect of the shortage of competent qualified staff, sample surveys of their treatment works show frequent non-compliance with the performance standards laid down. (For one example only: Snyman et al., 2006 ¹. And Figure 2.1 illustrates.)



Figure 2:1: The dysfunctional wastewater treatment works of a small town

Significant improvements would soon be seen if the generally under-qualified or under-resourced water services staff in these WSAs could have this ongoing support, mentoring and

¹ "The root cause for the poor performance at the majority of non-compliant plants does not seem to be the need for additional or upgraded plant infrastructure or the need for additional funding. The challenge is that the available plant infrastructure and equipment are not well operated and/or sufficiently maintained." (Snyman et al 2006, p11)

In terms of resources, "some form of intervention is required with regards to the following:

- Capital infrastructure investment at 85% of the plants;
- Skilled operational staff required to operate the plant efficiently at 50% of the plants;
- Skilled maintenance staff required to adequately maintain the installed mechanical/electrical equipment and instrumentation at 56% of the plants;
- Financial resources to support the routine operation and maintenance at 21% of the plants; and
- Information resources required to properly operate the plants at 63% of the plants.

The most pressing deficiency is the critical shortage of trained, skilled and experienced process controllers and mechanical/electrical maintenance staff." (ibid, p 4)

quality control – or if the WSA could enter into partnerships with microenterprises which would, through franchising partnerships, enjoy the necessary ongoing support, mentoring and quality control.

Given that the costs of the franchisor's higher levels of specialist expertise would be shared by several franchisees, the franchisor could afford to make this expertise available to each of them on an as-needed basis, and could provide other resources normally only available to larger water services providers. Access to this expertise would be of significant benefit to WSAs. (Figure 2.2 illustrates – although in this example the SMME is not a franchisee.)



Figure 2.2: A very much functional wastewater treatment works

At this treatment works, the operation and maintenance is outsourced by the owner, which also outsources the higher level skills that it requires in order to be a competent client

There is ample scope for the SMME private sector to assist, and there should be a range of ways in which entrepreneurship in water service provision can be encouraged and supported. Furthermore, if the entrepreneurs were not standalone enterprises, but were franchisees, they would enjoy competent franchisor support, and both franchisee and franchisor would be incentivised to make this arrangement work. Many useful pointers can be found in business format franchising's franchisee development programmes as well as in engineering infrastructure contractor development programmes, both of which have good track records in South Africa.

Whereas the municipal client's competence to monitor performance and enforce contract compliance is key to it effectively using the SMME sector, if a municipality is short of management resources, it would be putting these to more efficient use in managing the work of the contractor than in trying to cope with the operational issues itself. Given that there are currently not enough water services providers in South Africa, entrepreneurs should be offered the opportunity to assist with these operational issues.

Nevertheless, the argument for franchising partnerships as a means to improve efficiency in water services operation and maintenance does not depend on the case for or against the participation of for-profit organizations. There are already elements of franchising in some of the current activities of non-profit water services organisations in South Africa. For example, a valuable asset to several predominantly rural municipalities currently is the practice of appointing large water services institutions as "support services agents" to support water services providers that are NGOs and small, local CBOs. Although this arrangement is not franchising, development of the franchising partnerships concept has learned from the experiences of these, and they could in turn benefit from adoption of some of the characteristics of franchising.



Figure 2.3: The Drain Surgeon at work

It must be acknowledged that there are a few water services franchisors that have long been operating in South Africa. They are successful financially and in terms of the service (operation and/or maintenance of an element or elements of the water services delivery chain)

that they provide.² But they have not, or do not wish to, provide other elements, or provide their services to other than their current market niche (invariably private sector purchasers of their services). In more than one case, they would like to extend their services to WSA-owned infrastructure, but do not find the environment conducive.³ (Figure 2.3 illustrates)

Finally, while the case for water services franchising partnerships rests in the first instance on improvement of service delivery, through more efficient operation and greater reliability compared to the in-house operation or the standalone SMME, in addition to improving the service, the franchisee SMME stands a very good chance of making financial savings for the infrastructure owner. A simple example would be through effective pressure management – a lowering of the pressures at times when higher pressures are unnecessary, leads to reduced volumes of water wasted from leaks, and hence the municipality will at the end of each month receive a smaller bill from the bulk water supplier. Another simple example is that if pumps are maintained regularly and operated competently, they will invariably give longer and more reliable service, and need not be replaced as early as they would need to be if they were not being looked after.

3. Overview of water services franchising

The research has therefore been focusing on a partnership concept, making use of the principles of franchising, for improved water services infrastructure operation and maintenance, while ownership of the water services infrastructure remains with the public sector (e.g. the WSA).

The concept has been formulated with a view to improving water services operational quality and efficiency through introducing a new (to water services) supply-side operation and maintenance provider mechanism. (Figure 3.1)

The research has modelled the franchising of selected elements of the water services value chain.⁴

This modelling has drawn upon first-hand knowledge of the operation of these same elements in contexts close to franchising. It has also drawn upon understanding of the small number of franchises already active in the water services sector, and upon understanding of the very much larger number of franchises in other fields.

² For example, The Drain Surgeon is a well-known franchisor, based in Gauteng, but with franchisees under the same brand name in all major centres of South Africa.

³ Furthermore, much of the business information pertaining to these very few models is, understandably, guarded by the companies that possess it, and which have, with little if any exception, gained their information the hard way – through experience! It is their competitive advantage, and they are willing to share only up to a point.

⁴ See WRC Report TT 432/4/10 for modelling of:
A sustainable community-level caretaker management business;
a sustainable schools and sanitation business (Figure 3.2); and
a sustainable pressure control management business.

Other elements identified in that report for potential franchising partnerships included: leak detection, meter reading, demand management, plumbing services, management of abstraction points, laboratory services, data management, management of treatment package plants, management of municipal treatment works, and site and property management.



Figure 3.1: The type and scale of infrastructure that a small or microenterprise SMME franchisee could possibly operate and maintain

Many owners of water services infrastructure do not have the staff or systems to deliver a reasonable service. A carefully designed set of water services institution /franchisor /franchisee arrangements, efficiently implemented, could assist. At the same time, franchising partnerships offers opportunities to the SMME sector and to local economic development. Franchisees would be SMMEs – most likely microenterprises. But their association with a franchisor gives them considerable advantages – reflected in the support they enjoy and the guarantees of quality and reliability intrinsic to the franchisee's contractual relationship with the franchisor – and hence better service that they can provide – over standalone SMMEs.

All choices of institutions for water services delivery – whether of the primary water services provider (WSP) or (more feasibly) of subcontractors to that WSP – are between alternatives. The water services delivery model in common use (i.e. a heavy reliance on water services authority's/ municipality's own in-house resources) is not intrinsically flawed. The reason why many of the owners of the water services infrastructure and/or their appointed water services providers are not able to operate this infrastructure satisfactorily lies in the implementation of the model, rather than in the model itself. Given the too-often inadequate state of operation and maintenance of much water services infrastructure under the current institutional regime, water services authorities need to consider different and potentially more successful options, and to give serious consideration to adopting them, or at least facilitating their participation.



Figure 3.2: The "market" for a schools sanitation facilities operation and maintenance franchise

Franchising partnerships might not be ideal, but it might in many situations offer the prospect of improved operation and maintenance of water services. However three main priorities need to be addressed simultaneously if the operation and maintenance of public sector water services infrastructure is, in the cause of improved water services provision, and to the benefit of water services users, to be franchised where it is appropriate to do so. As follows:

- Ensure that the necessary steps are taken to allow the non-governmental organisation (NGO), community-based organisation (CBO) and SMME sectors to compete on even terms with in-house providers. At very least, this must be done where in-house operation and maintenance is showing obvious signs of serious or repetitive non-compliance.
- Address funding stream and municipal financial stability issues.
- Ensure that a few water services franchising pilots are up and running as soon as possible. These pilots will, through their success, demonstrate the potential of water services franchising partnerships.

National government is the key role-player in terms of addressing the first two of these priorities.

Water services infrastructure owners in the form of municipalities/WSAs are for the most part unlikely to change in respect of the first of these priorities. If, therefore, national government wishes to see change, it will have to demonstrate strong leadership.

Not many municipalities/WSAs are able of their own accord to bring about significant change in respect of the second of these priorities. Again, therefore, national government is going to have to lead. National government has already succeeded in bringing about some improvement, but much more needs to be done.

A “three-step breakthrough” is needed:

- The first step is the breakthrough to acceptance by water services authorities of outsourcing the operation and maintenance of infrastructure that they, the water services authorities, own. (To emphasise: this outsourcing need not necessarily be to the private sector – it could also be to NGOs and CBOs.)
- The second is acceptance that the institutions outsourced to could be SMMEs.
- The third step is acceptance that these SMMEs could be franchisees. (This third step should not be a problem once the second level of acceptance is in place.)

It should be considerably easier to convince clients of the merits of franchisee SMMEs than to convince them of the merits of SMMEs that are standalone.

Note that what is good or bad for SMMEs is good or bad for franchising. But the converse does not necessarily apply – or, putting it differently, a franchisee SMME, given the support it would receive from the franchisor, would in all likelihood find it easier to meet some regulatory and other requirements than would a standalone SMME, everything else being equal.

Chapter 4 puts in a nutshell the partnership concept, utilising the principles of franchising, for improved water services infrastructure operation and maintenance.

4. Water services franchising in a nutshell: A partnership concept, utilising the principles of franchising, for improved water services infrastructure operation and maintenance

In the briefest possible terms:

- The research has found that a franchise partnership concept can assist municipalities with their water services responsibilities, specifically the operation and maintenance of infrastructure.
- The municipalities will continue to own the infrastructure.

Water services franchising partnerships are a means of:

- assisting municipalities by providing the higher-level expertise in water and sanitation infrastructure operations and maintenance that would very seldom if at all be found outside the metropolises and larger urban areas; while
- creating and supporting CBOs and small entrepreneurs who can provide locally-based and thus efficient service provider solutions; and
- building local economic development.

The principles of franchising.

- Franchises’ success is based on replication of success, efficient logistics and a trained and capacitated workforce.
- Franchisee small businesses are easier to establish than standalone small businesses are.
- Franchising is robust, and able to ensure consistent quality products and services.
- Franchisees are obliged to adopt the tried and tested systems and procedures of the franchisor, and to accept the quality control of the franchisor – resulting in higher quality assurance and greater efficiencies.
- Franchises are able to innovate and develop constantly.

The concept addresses the lack of higher-level expertise that has so often been identified as a key to improvement of service, especially in the more remote areas. The local staff can deal with day-to-day operational needs, but are seldom able to deal with anything more demanding than that. The essence of water services franchising partnerships is: the creation of a pool of appropriate expertise upon which the local operators can draw; a restructuring of the local responsibility for operating; and the creation of a two-way obligation – an obligation to call for assistance from the pool, and an obligation to respond rapidly to that call. All of this together with the incentive structures to ensure that the partnership works smoothly. (For more detail, see second box alongside.)

The franchisees would be SMMEs (particularly SMME microenterprises) or CBOs. The franchisor would be any institution that has the required expertise, is willing to provide the service, and would not be in a conflict of interest by providing the service.

An analogy would be a combination of:

- a municipality (or any other owner) purchasing a motor vehicle together with a maintenance plan (or purchasing the maintenance plan afterwards); and
- the maintenance is undertaken by a franchisee, with the continuous support of a franchisor.

Finally:

- Franchising partnerships offer significant potential for improvement in services quality and reliability, greatly assisting the good functioning of municipalities.
- Franchising offers significant potential for the capacitation and participation of SMMEs – particularly microenterprises – and CBOs, and for BBEE.

Through franchising partnerships, matching skills levels, and matching obligations, together with incentives to use the skills appropriately and effectively.

- On most days at the (for example) treatment works, nothing extraordinary happens. Franchisee staff are able to cope.
- When major maintenance or upgrading is scheduled, or when there is a breakdown – those staff know who to call at the franchisor in order to bring the higher level of skill then, and only then, needed.
- And they know that the people they call WILL help, because there is a binding contract and a shared reputation.
- It is two-way obligation – an obligation on the franchisee to ask for help, and an obligation on the franchisor to give the help.
- Cost of the higher skills levels, which are needed only intermittently, is spread across many sites – thus cost per site is low.

5. Key findings from the research

Key points that emerge from the research are:

- If the WSP were a franchisee, this franchise alternative should not disturb present relationships between the WSA, other WSPs and others, but would simply add one more alternative to the array of possible WSP types.
- Whereas a WSA may require contractual recourse not only to the franchisee, but also to the franchisor, the franchisor could be a co-signatory to the contract or a guarantor of the performance of the franchisee.
- Selection of a site brings with it a WSA or another public sector institution that is the responsible authority for water services. In the initial stages of water services

franchising partnerships development, selection of an element of the water services value chain is likely to bring with it only a limited choice (or no choice at all) of a business model and a franchisor coupled to that model.

- Many potential sites for water services franchising already exist in South Africa, in the sense that much water services infrastructure is already in place but is not being operated properly at the present time. While these sites fall under the jurisdiction of or are owned by WSAs, and the reluctance of, or opposition of, what appears to be the majority of WSAs has been noted, a sufficient number of WSAs appear to be willing to consider undertaking, or permitting, water services franchising partnerships pilots.
- The sequence of events will probably be that franchisors will select water services elements and will formulate the business models to go with each. They will then look for sites to apply the models, and will seek the cooperation of the WSAs responsible. Finally they will offer the business to potential franchisees, or will attempt to nurture potential franchisees. As water services franchising partnerships in South Africa grows, however, the initiative may come from others – e.g. from the WSA, but to begin with it is highly probable that it will only be franchisors that initiate water services franchising partnerships proposals.
- Organisations will of their own accord elect to set up as water services franchisors. How much success they will have will depend on their expertise, resources and track record before entering water services franchising partnerships and once they are in it – and their acceptability and that of the franchising proposals they put together. This acceptability will be judged by key stakeholders, principally WSAs and financial institutions, but also by DWAF and by affected communities.
- The franchise industry literature over and over again advises against franchising a business without a business model that has been thoroughly worked through on paper and that has not been tested "in the field" over a period of time. As the Franchise Association of Southern Africa (FASA) manual emphasises, by far the best way to test the model is by "actually operating the business [this] is the only reliable way" (FASA 2005, p 60). This the franchisor should preferably do by for example running a directly-owned outlet that lacks only a franchisee and a franchise agreement, but has in place many of the other aspects of franchising – e.g. there would need to be an operating manual, training, quality control, etc.
- However the franchising of water services needs to exercise discretion in considering lessons from the established franchising industry. For example, a franchising partnerships alternative might in some instances be far preferable from the point of view of service delivery to the water services operation model being implemented at a site that is consistently not complying with laid-down water quality standards – even if the franchising alternative has not yet been fully formulated.
- A scan of South African franchising literature on franchising other than of water services found that franchisees need to have entrepreneurial attributes such as being highly motivated, hard-working, and willing to accept that the business may require months or even a year or two of building before profits can be taken. Specialist technical knowledge and/or operating licences are needed in some sectors.
- Future water services franchisees will probably be drawn from among the emergent independent operators already in the technology sector, or a franchisor's own employees, or community-based individuals or groups. Many (but by no means all) of these will probably need initial support from the franchisors or other external service providers or support services agents.

- It is anticipated that, for each potential franchising partnerships circumstance, a specific approach will probably be clearly enough evident at the time, and a pragmatic "horses for courses" attitude to franchisee selection will prove appropriate.
- Finally, a number of important issues need to be resolved before franchising partnerships to improve municipal water services operation and maintenance can become widespread.

One of these, clearly, is procurement procedures.

Another is budgeting – the SMME franchisee would need to be paid not the kind of budget that is so often allocated by a municipality to operation and maintenance, but would need to be paid the proceeds of a realistic, adequate budget.

Yet another issue is payment. No SMME can afford a delay of two or three months before it receives its due for services rendered, and it could go to the wall while it waits for payment by an inefficient municipal financial department.

A fourth issue lies in the essential services nature of water services – there has to be a backup contractual relationship between the franchisor and the municipality, that would oblige the franchisor to take over the franchisee's responsibilities, even if temporarily, should the franchisee fail for any reason whatsoever.

These key points are followed up in the rest of the current document, and especially in Chapters 6, 7 and 8. Chapter 6 describes generic (i.e. not specific to water services) roles and relationships in franchising. Chapter 7 describes water services functions that franchising partnerships can fulfil. Chapter 8 builds on Chapters 6 and 7, showing water services franchising partnerships institutional arrangements.

Specifically pertinent to the piloting that it is trusted will take place in the next few years:

- The participants in pilot implementation, and the sites where this piloting could be attempted, need to be carefully selected. If the pilot were to fail because of for example political or economic problems that would have defeated any service provider in the area, nothing about the merits of franchising partnerships would have been learned.
- Thus the selection of the initial pilot sites is principally constrained by the need to match:
 - water services infrastructure and site, and its environment, and
 - willing WSA and
 - willing and competent franchisor, preferably with local experience and local credibility (i.e. credibility built from a track record of delivery and of working with local authorities, communities and local small contractors); and
 - (once the above have been brought together) willing and competent potential franchisees.
- Further to that, a strong case needs to be made for doing the initial testing of the non-franchised business model in an area where, if the test result is positive, the first franchised pilot will be rolled out. This is the most direct way to establish:
 - local expertise (local management and staff) and
 - local familiarity with and confidence in the product (which in the case of water services should not just be confidence of the customers/end users, but of other stakeholders, especially of the municipality/WSA and of other WSPs).

As franchising partnerships spread, business models will proliferate, and companies with the appropriate water services skills and resources will be attracted to the franchisor role.

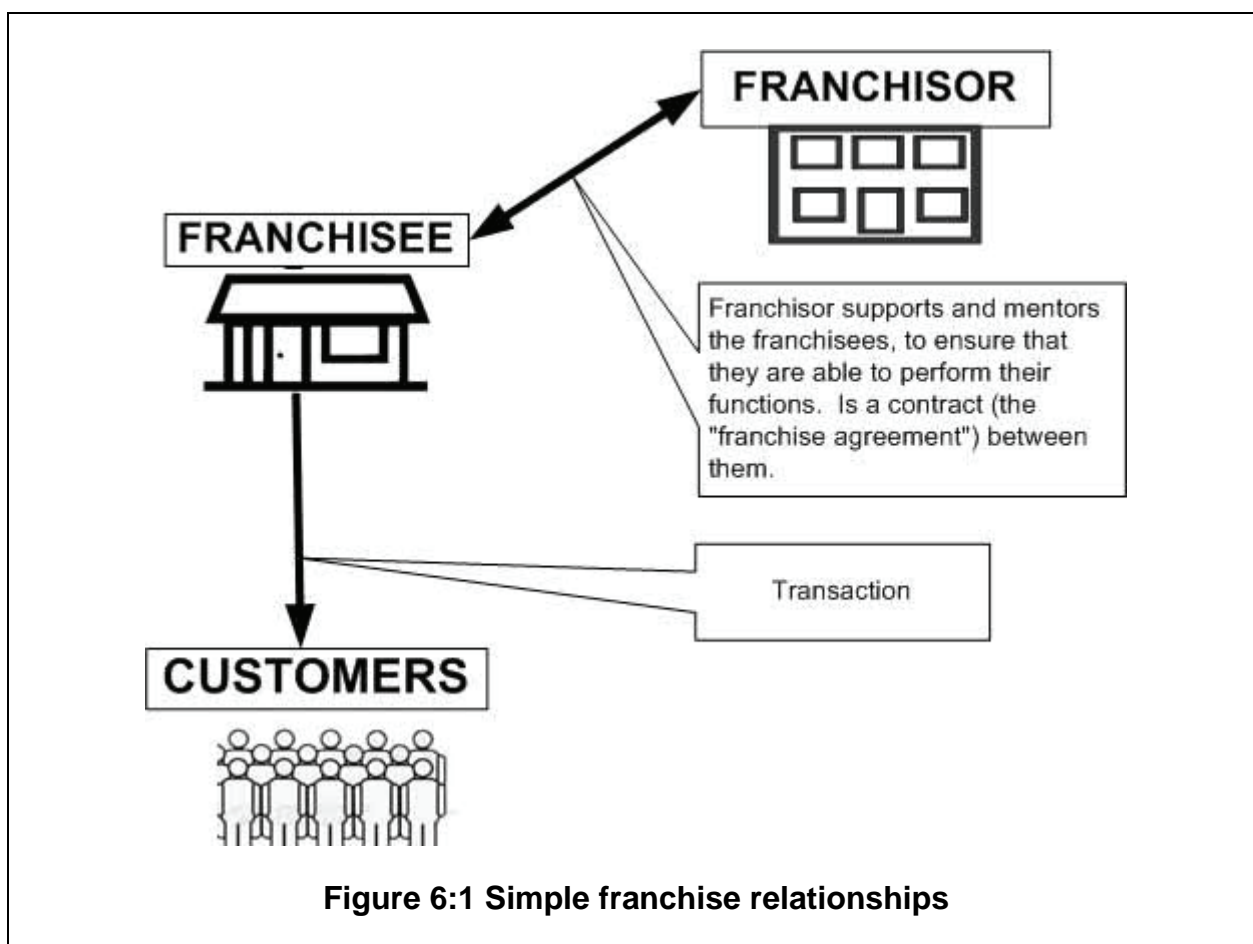
The documentation assembled as part of the study could provide a basis for experienced water services practitioners to at their own risk plan for and implement pilot projects. These experienced practitioners could also make use of these reports for assistance in motivating for the co-operation of WSAs, when selecting franchisees, and for other related tasks.

6. Roles and relationships: franchisor and franchisee

The context of the description of roles and relationships in this chapter is solely on franchising in general terms, aside of its application to the water services sector.

"Business format franchising" (to use its full name) is a business arrangement between a franchisor (the grantor of the franchise) and a franchisee (the recipient of the franchise). The two parties enter into an agreement with the intention to exploit the franchisor's **tried and tested blueprint of a successful business** for mutual benefit.

Thus the franchisor grants to the franchisee the right to use a business method or system, for which the franchisee pays fees. The assistance that the franchisor gives with setting up the franchisee's business, and the ongoing training and support of the franchisee and quality control of the goods or services, are usually also part of the agreement between them. There is in true business format franchising no direct contractual relationship between the franchisor and the customer/end user of the goods or services. Figure 6:1 shows the simplest form of this.



Franchising can be summed up in the slogan: “Being in business for yourself but not by yourself.”

Whereas the incentive to start up a small business is the prospect of a quantifiable financial outcome (profits, dividends or surplus), the presence of a successful business model that can be copied is the incentive to follow a franchise route as opposed to following a route without the support of franchising. These, the prospect of profits/dividends/surplus on the one hand, and on the other hand the model that can be copied and the reduced risk to the franchisee thanks to the support of the franchisor, are the twin driving forces of the franchise concept.

The following generic (and thus not specific to water services or to delivery of any other goods or services) description of the characteristics and roles of franchisor and of franchisee, and of some relationships, is a useful introduction to any further discussion.

A franchisor is an entrepreneur who has:

- Established a business in a clearly defined and growing market.
- Developed some unique product features or methods of delivery.
- Fine-tuned the systems and procedures necessary to facilitate ongoing customer satisfaction as well as the profitability of the business.
- Created a brand that enjoys some level of recognition and is well respected by suppliers and customers alike.

This entrepreneur is now ready to expand the business into a regional, national or even international network, but he or she knows that personalised service is the main reason for his success to date. As a result, he is somewhat reluctant to establish branches and entrust operational responsibility to employees. He wants to ensure that self-motivated individuals with a financial stake in the business take control of each new site.

He can select to become a franchisor in addition to, or in substitution for, any outlets that he personally runs (i.e. directly runs, as branches).

If he chooses to become a franchisor, he must make sure that his business is of a type that can be franchised. It might be that it is not suitable.

Following an in-depth review of all business processes, written guidelines for the optimal operation of the business must be drawn up and the necessary support infrastructure put in place, whereupon the process of franchising the business can commence.

A franchisee can best be described as an individual who wants to be in business but is reluctant to (or chooses in an instance not to) proceed on his or her own. The ideal franchisee:

- Should be a self-motivated individual who possesses the necessary drive to implement a proven system without requiring ongoing constant supervision, but also without questioning its merits at every turn;
- Must be a team player and prepared to co-operate in an enthusiastic, honest and proactive manner with franchisor representatives and the other franchisees in the network; and
- Should literally “live the brand” and identify with the network’s values.

People with a very high need to express their own individuality will generally not be happy as franchisees. Nor will franchising appeal to people who are expecting the franchisor to make all the decisions, do everything for them, and accept responsibility if things do not turn out the way they had hoped.

The relationship between franchisor and franchisee is governed by the franchise agreement. This should, with a minimum of legalese, clearly set out the rights and obligations of the franchisee and the franchisor.

7. Water services functions that franchising partnerships can fulfil

7.1 Operations and maintenance functions

It is not that the water services delivery model in common use (i.e. a heavy reliance on WSA's/municipality's own in-house resources) is intrinsically flawed, and that is why many of the owners of the water services infrastructure and/or their appointed WSPs are not able to deliver satisfactorily. Evidence that it is not flawed lies in that in many instances water services are being delivered satisfactorily, or more-or-less satisfactorily. It is in the implementation, rather than in the model itself, where the problems lie.

The franchising partnerships model for water services delivery has undoubted potential for assisting with the resolution of skills and incentives problems that are encountered by, or in, many WSAs and WSPs, or to structure alternatives to current water services delivery institutions. The model cannot, however, be expected to directly address a WSA's budget problems. Nonetheless, any measures that led to more reliable and sustainable water services would (for example through reducing wastage of water) result in cost savings to a WSA, thereby improving its financial situation.

Franchisee WSPs, dependent for their continued existence on the success of their business, have a strong incentive to perform, stronger than the incentive that in-house WSA personnel would usually have. Franchisees would also enjoy the benefit of the franchisors' expert guidance and quality assurance. On this latter point, a franchisor can ensure a professional approach, and provide quality control, ongoing training, as well as advice and help when needed.

This help from the franchisor would be of particular value to WSAs away from the major urban centres, few of which can afford to employ sufficiently skilled staff – which shows in the state of their infrastructure. Significant improvements would soon be seen if the generally under-qualified or under-resourced water services staff in these WSAs could have this ongoing support, mentoring and quality control or if the WSA could contract out some of their operations and maintenance responsibilities, entering into agreements with SMMEs that enjoy the necessary ongoing support, mentoring and quality control.

Given that the costs of the franchisor's higher levels of specialist expertise are shared by several franchisees, the franchisor could afford to make this expertise available to each of them on an as-needed basis, and could provide other resources normally only available to larger WSPs.

A WSA client's competence to monitor performance and enforce contract compliance is key to its effective reaping the benefits of appropriate outsourcing. Evidence is that the necessary competence cannot, sadly, always be taken for granted of many WSAs. However, if a client is short of skills, it would be putting these to more efficient use in managing the work of the contractor than in trying to cope with the operational issues itself.

If improved service delivery results in cost savings to the WSA and/or to improved service, this should improve the financial situation of the WSA, but in practice this financial improvement is

not always realised, and/or for other reasons the contractually obliged payments to the franchisee whose efforts have improved the service are not made, or not made on time. As a result of which the financial viability of the franchisee would be threatened. This is not easily resolved, and possible solutions, such as paying the franchisee directly from financial savings made as a direct result of the improved service, or the presence of a national government financial guarantor of last resort, might not be feasible or acceptable.

National government must, however, perceive that the franchise option has in a significant number of circumstances at least as good or maybe an even better chance of providing sustainable water services than any other option has. It would therefore be in the government's own best interests to facilitate the participation of franchised WSPs.

That a WSP, or a contractor to a WSP, is a franchisee rather than any other form of SMME or private sector partner, or a public sector entity, must not disturb institutional, financial and other relationships of the delivery model in common use. For example, in respect of funding, if equitable share is currently used to subsidise the water services to a set of households when the WSP is a municipal WSP, this must not change, and the same subsidy must flow, should the WSP be a SMME.

There are many situations where applying the principles of franchising could improve water services operation and management. Franchising appears to be advantageous in respect of some elements of water services delivery infrastructure, and in some circumstances, but not in respect of those same elements in other circumstances. Franchising should therefore be preferred in appropriate situations but not all situations are appropriate. As just one example: given the huge geographic areas that many municipalities cover, a locally based institution would have a distinct cost advantage over an organisation more centrally based in the municipality, and therefore at a greater physical distance and the customers would receive better service. Being a franchisee would ensure that it could access higher levels of expertise when they were needed.

7.2 Infrastructure investment functions

It is for good reason generally understood that franchising is not suitable for investment in new infrastructure.

Certainly, the amounts of funding required for investment in new infrastructure, or even just the reconditioning or refurbishing of it, would be beyond the means of all franchisees (SMMEs that they are, and generally at the "very small" and "micro" end (that is, turnover less than R 2 million per annum)). Investing in new infrastructure would even be beyond the means of many franchisors. Over and above these concerns, there would be an understandable reluctance on the part of franchisees and franchisors to invest capital in infrastructure given what appears to be an environment of uncertainty as to whether they will be able to recoup the cost of that investment. (Limited capital investment is nonetheless occasionally made.)

Either way, it seems to be justifiable that, in the current climate, potential franchisors and franchisees regard capital investment as an option to be considered only in exceptional circumstances. With respect to the provision of public services infrastructure, franchising is almost invariably regarded as suitable only for the ongoing operation and maintenance of infrastructure.

7.3 How do franchisors and franchisees get selected – or select themselves?

If, and only if, the three-step breakthrough⁵ can be achieved – and it need only be in respect of a sufficient number of circumstances (e.g. a WSA that is willing to allow a pilot water services franchising partnership) – can water services franchising partnerships be contemplated. In which case, an early question that will arise will be that of how franchisors and franchisees get selected, or select themselves.

For current purposes, where the franchising of the operation and maintenance of public sector water services infrastructure is almost unknown, discussion must be in the context that the water services sector has, even if only in limited circumstances, no more than proved open to franchising partnerships. Which partnerships would initially have to be on a pilot scale.

Given that in the context of the current study the "business" is the operation of an element or elements of the water services value chain, the choices available in respect of each of element/business, franchisor, franchisee and area/site, are likely to be limited initially, for reasons noted below.

In the early days of water services franchising, at least, it is most likely to be franchisors that will initiate a process, selecting water services elements most suited to them, and will formulate the business model to go with each selected element. They will then look for areas or sites where this expertise is needed, and will negotiate with the WSAs and other role-players. Next they will offer the model to potential franchisees, or will attempt to nurture potential franchisees and offer it to them. All the while, the usual procurement practices (by WSA and others) will apply.

As water services franchising partnerships in South Africa grows however, the initiative to take the franchise route may come from others – e.g. from the WSA. But to begin with it is highly probable that it will only be franchisors that initiate water services franchising partnerships proposals.

Selection criteria – sites, franchisors and franchisees

Selection of the initial sites will be principally constrained by the need to match all of the following:

- water services infrastructure and
- sites, and their environment, that are not fraught by for example ongoing political unrest or dire poverty, and
- willing WSAs and
- willing and competent franchisors – best of all if with local experience and local credibility (i.e. credibility built from a track record of delivery and of successful working with local authorities, communities and local small contractors).

There are already many existing potential sites for water services franchising partnerships – "already existing" in the sense that much of the water services infrastructure already in place is not being operated and maintained properly at the present time. While these sites fall under the jurisdiction of or are owned by WSAs – and despite the reluctance of what appears to be the majority of WSAs to consider franchising, or even any outsourcing of operation and maintenance – a sufficient number of WSAs appear to be willing to consider undertaking, or permitting, water services franchising partnerships pilots.

⁵ See Chapter 3.

It should not be difficult to find sufficient sites from which to select in order to undertake an initial small number of water services franchising operation pilots.

Organisations can of their own accord elect to set up as water services franchisors. How much success they will have will depend on their expertise, resources and track record – both before entering water services franchising and once they are in it – and their acceptability and that of the franchising partnerships proposals they put together. This acceptability will be judged by key stakeholders, principally WSAs and financial institutions, but also by DWAF and by affected communities.

"Selection of franchisors" implies that there will be franchisors to choose from. However there is unlikely to be much choice in respect of water services, simply because way into the foreseeable future there will be few franchisors in this sector – water services franchising partnerships is unknown to all but a few potential franchisors.

A franchisor's proposal rests on the soundness of the business model offered. The franchise industry literature time and time again advises potential franchisors:

- do not franchise a business without having a business model that has been thoroughly worked through on paper; AND
- do not start franchising without testing the business model "in the field" over a period of time.

In order to as thoroughly as possible prepare for a potential water services franchising partnerships opportunity, a strong case can be made for testing the non-franchised business model in the same area that, if the test result is positive, the first franchised pilot will be rolled out. This is the most direct way to establish:

- local expertise (local management and staff) and
- local familiarity with and confidence in the product (which in the case of water services should not just be the confidence of customers/end users, but of other stakeholders, especially of the municipality/WSA and of other WSPs).

Ideally the franchisee would be a person with a stake in the community of the area to which he or she then provides the service, who has social as well as financial goals, and who would be responsive to the needs. Having said that, the constituency from which many franchisees will be drawn will probably be not much dissimilar to the population from which both small water services operators and non-water franchisees are presently drawn. That is, the constituency will generally be either:

- emergent independent operators already active in the water sector, or
- franchisor's own employees, or
- community-based groups or individuals, or
- local businesspersons looking for additional opportunities.

Many (but by no means all) of these franchisees will probably need initial support from the franchisors or other external service providers or support services agents over and above the support usually, in conventional franchising, expected of a franchisor.

Selection of water services franchisees on the basis of the view held generally in the conventional franchising sector, that franchisees must be hungry to succeed and make money, would be at variance with suggestions that franchises be allocated on any other basis whatsoever – e.g. if that basis were representivity of a community. However there will probably not be a need to confront the differences between the kind of hard-headed commercial measures that conventional franchising stresses, and a softer approach. No doubt for each potential franchising partnerships circumstance a specific approach will be clearly enough evident at the time, and a pragmatic "horses for courses" attitude to franchisee selection will prove appropriate. Time will demonstrate this one way or the other.

Finally, a caveat: The franchising of water services needs to exercise discretion when considering lessons from the established franchising industry. For example, a franchising partnership's alternative might from the point of view of service delivery be far preferable to the water services operation model than being implemented at a site, if that model is consistently not complying with laid-down quality standards. Even if the franchising partnerships alternative for the particular operation has not yet been fully formulated, and bearing in mind the usual imperative not to launch franchising until a model has been thoroughly tested, it might be that other needs override – it might be that there is a need to replace the current model at almost all costs. Great caution must however be exercised – water services franchising partnerships cannot afford to get a reputation of failure, even if that reputation is undeserved.

8. WSP franchise institutional arrangements

8.1 Franchising in the water services sector

8.1.1 Introduction

Broadly, a franchise is the granting of a right, together with obligations, for a specific purpose. Thus, in respect of water services, who might be the franchisee, who the franchisor, and what is being granted?

Consider first the roles of and the relationships between the WSA and the WSP irrespective of franchising of water services even being contemplated. The context, as repeatedly stated in the documentation from this study, is invariably limited to operation (including maintenance) of water services. (Bearing in mind the legal prohibition placed on private sector ownership of existing water assets, the WSA must retain ownership, at least of existing assets. If new assets are required for a part of the area, there remain complications and limitations in mobilising private sector investment, including lengthy selection processes, commercial unattractiveness and low financial returns in small or peri-urban communities. So it is assumed, for the purposes of all discussion in the current document, that the WSA must provide these infrastructure investments.)

8.1.2 The WSA and the WSP

There is in the water legislation a clear difference and separation between the roles and functions of the WSA and WSP. This concept of separate roles, initially codified in the Water Services Act, was an important step forward in the industry for many reasons. An important role of the WSA is one of contracting a WSP to operate a water system in its area, subject to the authority and policies of the WSA.

Thus the WSA is responsible for providing water services to all in its area of jurisdiction. A WSA may contract with one or more WSPs. The WSPs may be the WSA's in-house WSP, or a utility, or a NGO, or a private sector operator retained under contract, or another option. Figure 8:1 refers.

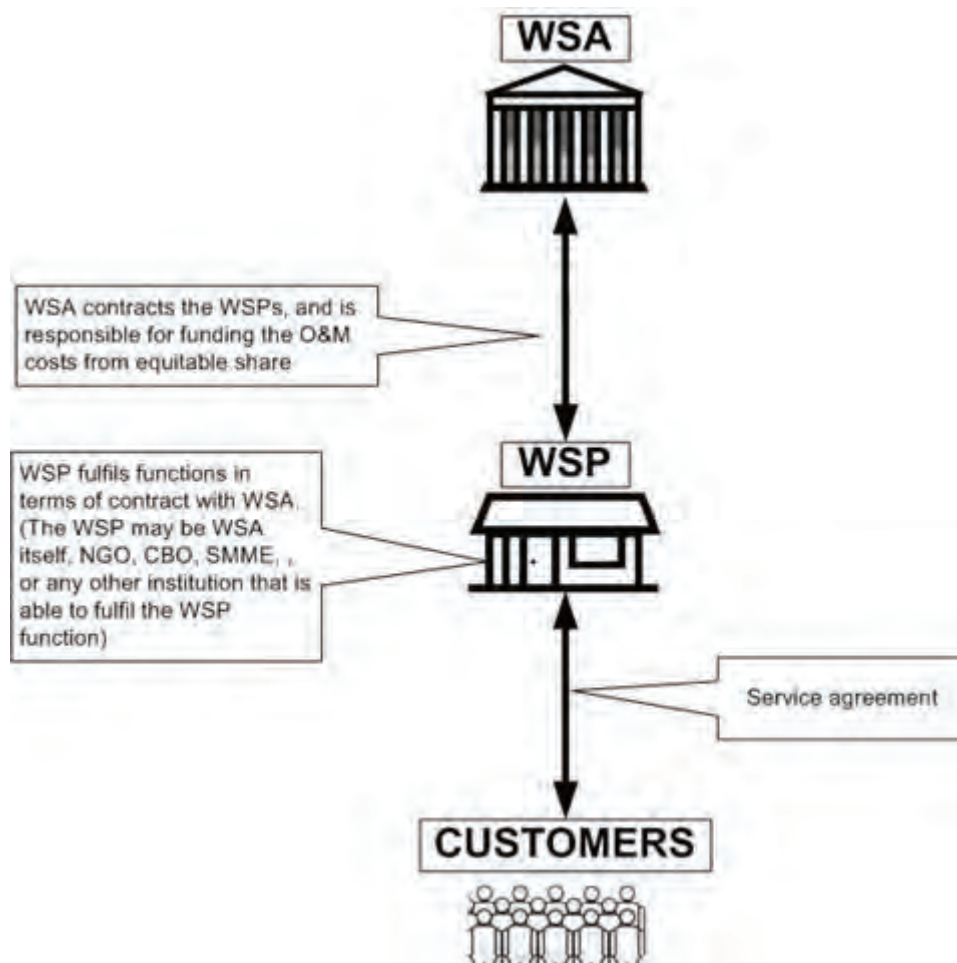


Figure 8:1 Water services sector contractual relationship

Note that in practice it is unlikely that a SMME, especially if a microenterprise, would be a WSP directly contracted to a WSA. The small size of SMMEs counts against them. In nearly all conceivable circumstances, the WSA will contract with one or a small number of "prime" WSPs in its area, and these will in turn contract with smaller "sub-WSP" WSPs – including the likes of CBOs and SMMEs.

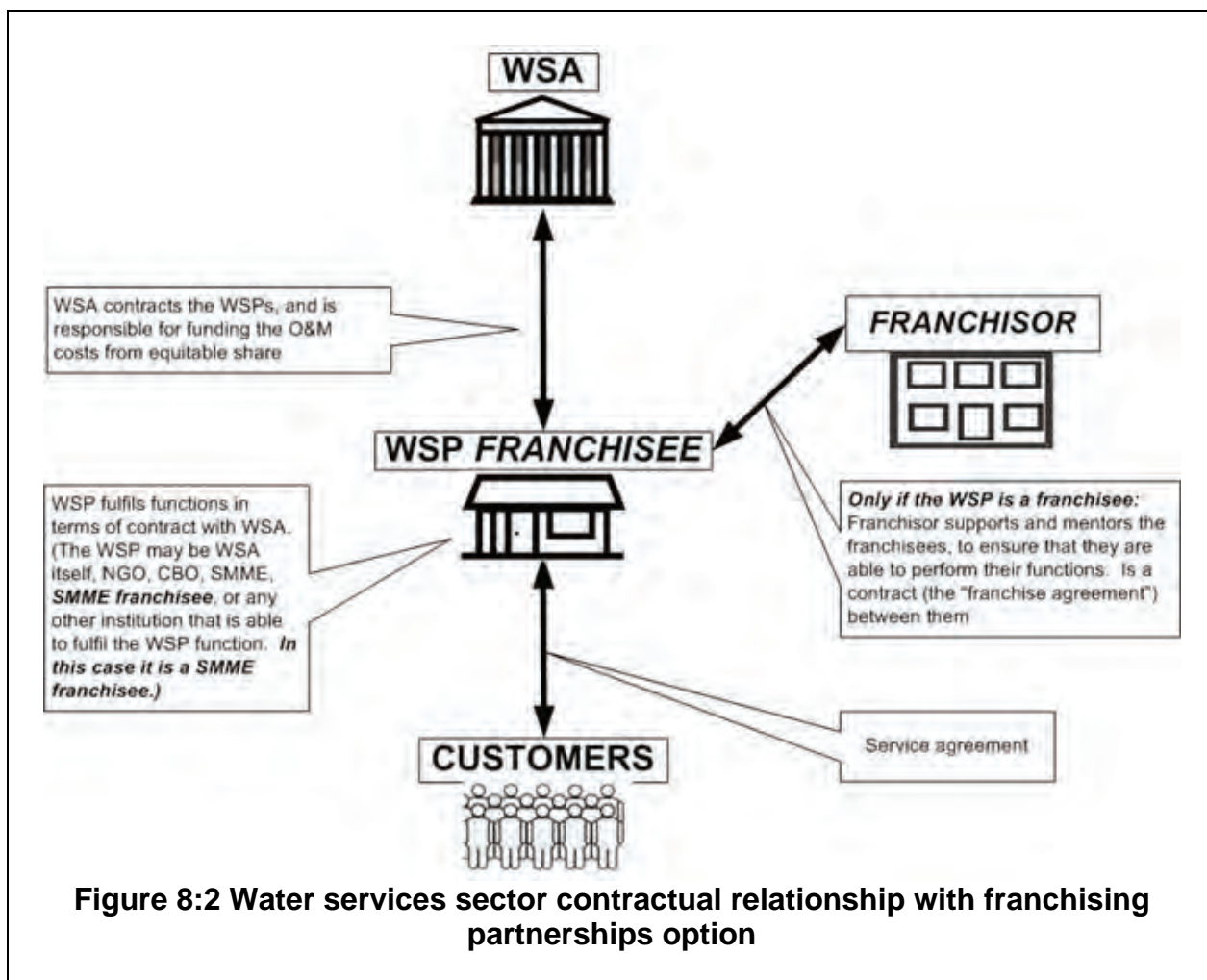
8.1.3 Water services franchising partnerships

The franchisee would be an entity that would be contracted, either directly by the WSA or by a WSP, to provide a component of the service delivery function.

Bear in mind that (as far as the current authors are able to find out) there is no such company or franchise structure active in this sector. ⁶

⁶ Franchisors such as The Drain Surgeon and PWMSA contract almost exclusively with private sector owners of infrastructure, and not with WSAs or WSPs.

The 2005 report showed (Wall 2005 – Figure 7.2, page 75) how, if the WSP were a franchisee, the franchise alternative would not disturb the present relationship structure. It would simply supplement it, adding one more alternative to the array of possible WSP types. Figure 8:2 illustrates.

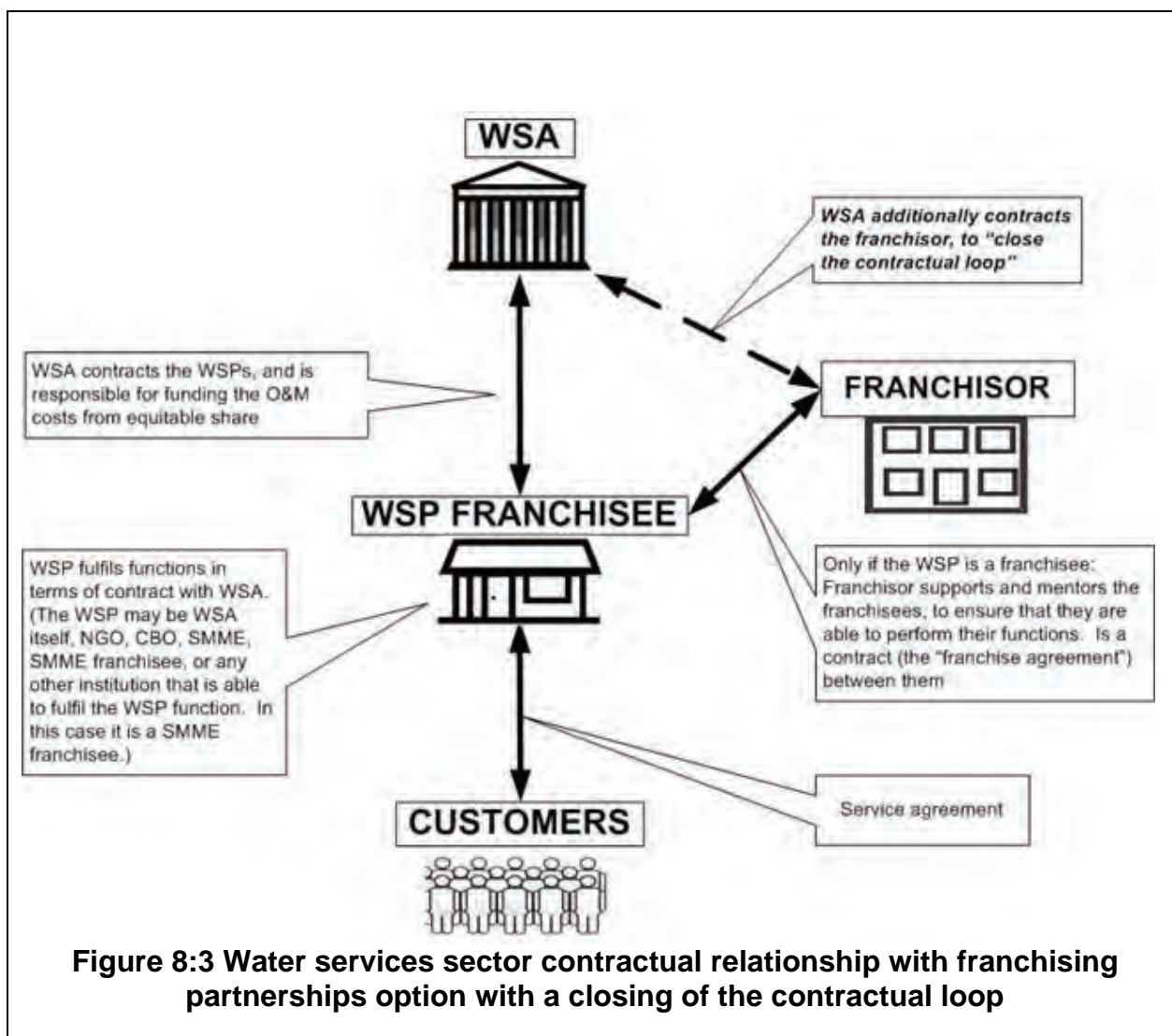


It is clear from a comparison of Figures 6:1 and 8:1 with Figure 8:2 how franchising (Figure 6:1) adds to the water services sector non-franchising contractual relationships (Figure 8:1) without removing any of the non-franchising contractual relationships, the result being the water services sector contractual relationship with franchising partnerships option. (The franchising elements are highlighted in bold italic in Figure 8:2.)

Whereas a WSA may require contractual recourse not only to the franchisee, but also to the franchisor, the franchisor could be a co-signatory to the contract or a guarantor of the performance of the franchisee. This "closing of the contractual loop", if it were deemed to be necessary, would require an additional contract, one that closes the loop between the franchisor and the WSA. The WSA may require contractual assurance that the franchisee will be supported by strong management, and that the franchisor is able to make alternative arrangements that will ensure continuity of service should the franchisee fail to meet its contractual obligations to the WSA.

Especially this could be necessary if the franchisor's expertise or track record is a significant reason for contracting with the franchisee, and the franchisee is a largely unknown quantity.

Figure 8:3 illustrates. (The elements added to Figure 8:2, to make Figure 8:3, are highlighted in bold italic.)



8.2 The client, the regulator and the contract

Briefly, if it is not already clear, to consider who would be the client, and also to consider would be the regulator. Also how long the contract could be.

The client of the primary WSP would under most circumstances envisaged be the WSA. As always, this would be the owner of the water services infrastructure. SMME franchisees however would under almost all conceivable circumstances be subcontractors to the primary WSP.

The regulator, i.e. regulator of the performance of the SMME, would be the same as the regulator for all water services, that is, DWAF. There is no need for a regulator as such of the SMMEs – the WSA or other infrastructure owner is regulated by DWAF, and it is up to the WSA to ensure that its WSPs and their subcontractors perform adequately, so that it, the WSA, does not fall foul of the regulator. Given that, a SMME would not be regulated as such – how well it performs would be governed by its contract with its client.

Issues such as the determination of tariffs do not come into the picture at all. These are matters that the WSA or other infrastructure owner is solely responsible for. There is, or should be, a firewall, i.e. the contract, between the WSA and the WSP, and the WSP is not in any way involved in tariff-setting.

Finally, on the topic of how long the contract should be. To ensure that the franchisor and franchisees continue to provide good quality, affordable services, and grow and improve the business, the franchise contract would need to be between five and ten years. One possibility is that the respective contracts be open to competition every ten years for the franchisor and every five years for the franchisees. These would allow sufficient time for both parties to recover their initial investment and also encourage them to perform well so that they would be re-awarded their contract for a further term.

9. Policy and statutory considerations

9.1 Pertinent national water services and procurement legislative implications

9.1.1 Introduction

Policy and statutory considerations, and financial considerations, largely determine the environment within which the water services sector functions. Considerations significant to partnerships, particularly if the one partner is a SMME (including SMME franchisee), are set out in this chapter and the next – policy and statutory considerations in Chapter 9, financial considerations in Chapter 10.

9.1.2 Statutes, regulations and policies

The following statutes, regulations and policies are those most relevant to water services franchising partnerships:

- The Water Services Act (South Africa 1997) governs the approval of water services providers.
- Water Services Provider Contract Regulations set out the contents of WSP agreements. These regulations thus provide a scope or check list for the contractual relationship between the franchise operator and the municipality.
- Sections 76 through 82 of the Municipal Systems Act is the most authoritative set of requirements that must be observed by municipalities in determining mechanisms for the procurement of service providers.
- The Department of Provincial and Local Government (DPLG) compiled the Green Paper on Municipal Services Partnerships (MSPs) in order to create a policy environment that enhances the viability and feasibility of MSP service delivery..
- The Local Government Municipal Finance Management Act (MFMA) stipulates conditions to be complied with and processes to be followed when entering into public-private partnerships:
 - The MFMA requires that a municipality must show, through a feasibility study, that a public-private partnership is superior to an in-house approach to providing the service before entering into such a partnership.
 - The MFMA also stipulates requirements for services (and goods) contracts procured by municipalities.
- The governance of companies is primarily regulated under the Companies Act.

A very significant challenge to outsourcing, especially outsourcing to SMMEs, is the financial state of many municipalities. (But that state is just as much a challenge to the municipality trying to deliver services using its own staff.)

Legislation requires that a municipality undertakes a feasibility study to compare the private sector option with an in-house option before procuring a MSP. The main policies, legislation and regulations that guide procurement of providers are:

- The Water Services Act sets out requirements that must be observed by WSAs before entering into contracts with private sector water services providers.
- DWAF has published a “consolidated guideline” for selecting water services providers. These guidelines amplify Sections 78 to 81 of the Municipal Systems Act.
- The Green Paper on MSPs describes the feasibility study required before appointing, or entering into an MSP.
- The Municipal Systems Act (South Africa 2000a) sets out a competitive bidding procedure that must be followed in procuring an external service provider, if the decision is taken to follow the external provider route.
- The MFMA (South Africa 2003b) sets out requirements that must be complied with before municipalities may enter into contracts that have future budgetary implications.
- Additional procurement requirements for public-private contracts are set out in Municipal Public-Private Partnership Regulations. (South Africa 2005)

The key pieces of legislation governing BEE and preferential procurement are:

- The Preferential Procurement Policy Framework Act (South Africa 2000b); and
- The Broad-Based Black Economic Empowerment Act (South Africa 2003a), which aims to promote economic transformation in order to enable meaningful participation of black people in the economy.

9.1.3 Inferences

Inferences with respect to the possible outsourcing and procurement of water services operation and management, but not specific to franchising, can be summarised as follows:

The study found nothing in national policy, legislation or regulations preventing outsourcing of water services operation and management. ⁷ (This outsourcing can be a public-public partnership or a public-private partnership, or a partnership with a non-governmental organisation (NGO) or community-based organisation (CBO).)

However numerous requirements must be met before any aspect of water services operation can be outsourced. Municipal service or management contracts need to be procured in accordance with the legislation and regulations. Even contracts that appear to fall within DWAF's Water Services Act relatively narrow (compared to that in legislation originating from National Treasury and DPLG) definition of procurement by a water services provider do still have to conform with the rules for procurement by private sector municipal service providers or external providers in terms of Sections 76-82, and especially Section 78, of the Municipal Systems Act.

Legislation relating to procurement by municipalities mainly relates to procurement of private sector service providers. The rules relating to feasibility studies etc do not all apply where the services of public sector providers (e.g. water boards) are procured.

The municipality must make the effort to undertake the Section 78 process before it can consider outsourcing. However a municipality is not required to demonstrate that it can provide the service in-house better than any outsourcing could do. This must be challenged.

⁷ Given belief to the contrary in some quarters, it is as well to emphasise this.

In practice, few municipalities feel applied obliged, in the interests of their citizenry, to go to the trouble of seriously considering alternatives to in-house, and thus only a minority of municipalities do make the effort. The current authors feel that all municipalities must be encouraged to undertake Section 78 investigations in order to determine to what extent they are able to best carry out their responsibilities in-house – and thereafter to determine to what extent they should outsource as opposed to what extent they should use in-house service provider solutions. By denying themselves the opportunity to explore alternatives through an objective Section 78 process, these municipalities may have no reliable financial or information-supported rationale for the decisions they need to take in the interests of improving services to their customers.

The bias evident in many municipalities against the procurement of private sector, NGO and CBO water services providers cannot be addressed through legislation or regulations – it can only be addressed by clear political leadership.

A major potential source of information, and also a regulatory tool, is the water services audit which should be enforced by DWAF.

Legislation does not, once a municipality has decided that it is prepared to accept outsourcing, prejudice SMMEs. In fact, the procurement legislation favours small procurements – particularly, procurement of service providers offering services for contracts under R200 000 is simplified. (Procurement of service providers for all contracts of a value above R200 000, regardless of whether SMME, CBO or NGO, and BEE or not, must be in accordance with the municipality's supply chain management policies compiled in accordance with National Treasury regulations.)

Company legislation gives important guidance for the screening of potential MSPs.

There are indications that unions will resist any form of what they perceive to be outsourcing of municipal service provision. They would do this on the debatable grounds that it could lead to retrenchment of their members.

Inferences specific to the franchising of water services can be summarised as follows:

The policy, statutory, and regulatory regime with respect to water services franchising partnerships is a subset of the wider environment determining and controlling WSPs. Franchisees are SMMEs of a particular type, and SMMEs in turn are part of a wider private sector, so anything that affects outsourcing (that is, outsourcing not just to the private sector) would affect franchising as well.

There appears to be nothing in policy, legislation or regulations preventing franchising partnerships of water services.

That franchising is not specifically mentioned in the procurement-related material that is reviewed in the current document would seem to be only because national government has regarded it unnecessary to have specific provisions relating to franchising.

DPLG, National Treasury and DWAF support will be required for the franchising approach.

The more capacitated of the water boards could be in a good position to fulfil the role of franchisor.

Policies, statutes and regulations favourable or unfavourable to operation and maintenance of water services infrastructure by SMMEs are also good or bad for operation and maintenance by franchisees. But the converse does not necessarily apply – or, putting it differently, a

franchisee SMME, given the support it would receive from the franchisor, would in all likelihood find it easier to meet some regulatory and other requirements than would a standalone SMME, everything else being equal.

The franchise approach does have the potential to substantially lever up the black ownership component of the contractor through a real contribution by the franchisee, and is clearly not fronting.

9.2 Franchising implications

South Africa does not have specific franchising legislation. This does not mean that franchising operates outside the law – it simply means that general legislation and precedents, arising from common law principles and from statutes that deal with commercial agreements, provide the legal context to franchising activities.

Franchising has been the subject of much litigation – inevitably, these cases are drawn from outside the water services sector, as there is no experience of franchising within the water services sector in South Africa.

FASA has listed the most important elements of franchise documentation.

The most important document is the contract between the franchisor and the franchisee (the "franchise agreement"). This sets out the rights/obligations of franchisor and franchisee respectively, "although the franchise agreement should strive for an equilibrium between rights and obligations as far as possible, the network's needs dictate that the franchisor's rights must be stronger in certain respects, to ensure control". (FASA 2005, p 49)

FASA cautions that "for a franchise agreement to be effective, it needs to be tailored to the needs of the business and the circumstances surrounding its operation. ... the drafting of a franchise agreement does not lend itself to a do-it-yourself approach." It would be asking for trouble to "copy an agreement that was originally drafted for a different network". (ibid, p 50)

The other three main types of "essential franchise documentation" comprise –

- the operations and procedures manual;
- set-up and training manuals; and
- the disclosure document. (This latter "explains the entire franchise package, including the legal and financial implications, to the [franchisee] prospect.") (ibid, p 48)

10. Financial considerations

10.1 Introduction

Income streams must be sufficient, or the participation of the CBO, NGO, SMME, franchisor or what-have-you will not be sustainable. This chapter addresses a number of financial issues, including the infrastructure owner's budget for water services operation and maintenance, and the income streams to the operators – but the emphasis is on the latter.

The financial affairs of many WSA/municipal owners of water services infrastructure are not in order. Many medium and low capacity municipalities are unable to report on their financial status. Inability to always follow acceptable accounting and payment procedures, including inability to process invoices and pay them on time, is much in evidence. Many municipalities are not able to recover all of the revenues due to them – sometimes they cannot even recover

most of the revenues due to them. This does not bode well for CBO/NGO/private sector involvement in the provision of water services, because:

- CBOs, NGOs and private enterprises will only survive if they are paid.
- If municipal inability to process invoices and pay them on time presents considerable problems for outsourcing even to larger municipal services partners, it would very likely be fatal to SMMEs, especially if microenterprises, which have much less (maybe minimal) financial resources and might be dependent on only a few clients or even on only one client.
- It is unlikely that others will be able to collect revenue on behalf of the municipality if there is no political will to support such efforts.

10.2 Funding streams for water services SMMEs

The certainty and reliability that they will be paid for their services has to be prominent on any checklist of the issues that need to be weighed up by CBOs, NGOs and SMMEs (and their bankers and sponsors) when they consider contracting to supply operation and maintenance resources to a municipality in its role as a WSA – or even when they consider subcontracting to a third party that is contracted to the WSA.

If the funding is promised, will it be budgeted – and if it is budgeted, could that budget be cut – and even if the budget as such remains firm, will the funds be paid? Could the funds be diverted to other purposes? Could payment be subject to delays? What would consequences be? Why would these things happen – and what can be done about them?)

SMMEs offering operation and maintenance services to the public sector could be dependent on a single client for their existence. If this client fails to pay on time and in full, that could be disastrous for the SMME. One client not paying it for 30 or even 60 or more days would be a nuisance to a large enterprise with a large spread of clients, but for a microenterprise, its main or, worse, sole client not paying it for even 15 days could ruin it financially.

Small businesses unable to meet their obligations, because their clients do not pay them or any other reason, simply close down, and the entrepreneurs move on. This sounds harsh, but it is reality. Larger businesses lay off workers and downsize.

The structural flexibility of the private sector can greatly improve the efficiency of local government. If all the municipal services were provided in-house, when the budget is frozen or the revenue stream dries up, the municipality must continue to employ and pay an underutilised and unproductive work force. That the budget which is available would under most circumstances go to salaries rather than to other disbursements, such as fuel or spare parts, would lead directly to cost to the ratepayer / fiscus without productivity.

While this flexibility constitutes another strong argument for municipalities/WSAs to consider outsourcing, it threatens the viability of the small enterprises contracted to them.

Even if the municipal client meet its contractual obligations to the letter, another dimension is that the problem with any funding provided by a municipality is that they can assure funding for only one year, but probably not longer than that – not even into the medium term.

One supplier put it as follows (paraphrased): “You can train plumbers, but next year they have no work to do. It is financially viable for The Drain Surgeon to set up and train franchisee plumbers, because his customers in the more affluent areas and the commercial and industrial areas will always have money to pay for the service – they are not dependent on municipal budgets. If he were to extend his service into the townships, even with municipal guarantees, that guarantee would only be for one year, and we already know that the householders in the townships cannot pay from their own wallets for his services. A viable business needs

assurance of at least a minimum amount of revenue in future years. And given also that our municipalities focus in the year or so preceding elections on impressing voters with development above the ground, that year there will be even less money for maintenance than usual.”

There is a dire need for management, operation and maintenance services partnerships, especially if these protect the revenue base that sustains municipal services. That notwithstanding, capacity problems in many municipalities, and the poor record of payment for contracted services that is too-frequently encountered, are substantial threats to suppliers to municipalities, and especially to SMME microenterprises, because they do not have substantial resources, may be heavily dependent on one municipality for their livelihood, and other reasons.

10.3 Conclusion on funding

Neither of the preceding sections has been specific to franchising – both have referred to funding issues faced by CBOs, NGOs and SMMEs.

The study has however amply demonstrated that franchising of water services has great potential to improve efficiency and provide municipalities with access to capacitated resources at the operational level. Thus ways to overcome the funding problems must be found – and they can be. Franchising, as pointed out before, gives franchisees an inbuilt advantage over standalone SMMEs. Franchises can for example support franchisees in their attempts to be paid as contracted – by exerting pressure on clients to release unjustifiably withheld payments.

Importantly, the attention of national government has recently most forcefully been drawn to the budgeting for operations and maintenance, and to the stop-start release of these budgets. Government is considering addressing this by various measures. In particular, the National Water Services Infrastructure Asset Management Strategy of DWAF has been considering a range of measures that will improve funding and budgeting for infrastructure asset management – particularly the amount, prioritisation and assurance of that funding. Also, the first (of four) "thrusts" of the National Infrastructure Maintenance Strategy is concerned with planning and budgeting for infrastructure maintenance. (Public Works et al., 2006, pp 13-14)

11. Critical success factors for franchised water services partnerships

11.1 Generic key success factors and causes of failure

The context of the discussion in this section (11.1) is franchising in general terms, aside of its application to the water services sector – nonetheless the comments apply also to water services franchising partnerships. The next section (11.2) covers franchising as applied to the water services sector.

The following summaries of key success factors and of principal causes of failure are of value in further defining the characteristics and roles of franchisor and franchisee, and the relationships between them. All are highly pertinent to selection of franchisor, franchisee and area/place of the franchising venture.

These key success factors include, principally:

- Franchisor has an existing successful business to study, model and systematize.
- Clear definition and understanding of the product, the customers and the market.
- Simplicity and replicability through systems (i.e. personality cannot be replicated, but systems can).
- Local applicability of the concept. (Some concepts cannot be exported for a variety of reasons, including cultural reasons.)
- Training (and retraining) schemes.
- Franchisee understands franchising and his roles and functions, and can manage his expectations.
- Franchisee has some commercial background or a culture of trading.
- Franchisee puts some equity into the business.
- Franchisor invests in the franchisee.
- The franchisor/franchisee relationship is sustained for the planned franchise period.
- The local community accepts the franchise concept and this particular franchise.
- The local community accepts the particular person of the franchisee.
- Continuous franchisor support of the franchisee: including redesign, market research and quality and performance audits.

Principal generic causes of failure are usually one or more of the following:

- Wrong business:
Not all businesses are automatically sound and attractive to investors and entrepreneurs. There must be sufficient income for the franchisee and franchisor, not only to live on, but also to justify the risk and extra hard work needed to get established in the first place. There will in any community be competition between business opportunities for entrepreneurs and investment. If the duration of the lease is to be short, there will be even greater pressure to make money while the lease is current.
- Unfranchisable business:
Not all business types can be copied and systematised simply. The systems are the key to replication. In some instances the personality of the founder is a key. In others there may be an indefinable aspect of the business that makes a difference to the customers or investors.
- Unsuitable site or location:
In property, "location, location, location" are the three key determinants of value. Many franchised businesses are no different.
- Wrong people:
Entrepreneurs must have tenacity, commitment and zeal. Education alone is not a sufficient indicator of suitability. This applies equally to the franchisor and franchisee.
- Lack of understanding of the product and the market:
Both franchisor and franchisee must fully understand the franchise systems, and these systems must be reflective of the business needs.

To sum up: the success and failure factors cover issues inherent both:

- in the selection of businesses, on the one hand, and
- in the selection of franchisors, franchisees and geographic areas on the other.

11.2 Water services franchising key success factors and causes of failure

The context of the discussion in this section is franchising in the water services sector.

All of the factors noted in Section 11.1 apply. However additional factors would apply to water services franchising partnerships.

Whether the environment is conducive to partnerships is a major consideration. Without a sympathetic environment, franchising partnerships will not get past the planning stage. Public sector owners of water services infrastructure (e.g. WSAs) need to see the benefits of utilising SMMEs – especially of utilising microenterprises – compared to trying to employ their own staff to do the work. Their seeing this will only come about through firstly their being lobbied (e.g. by potential franchisors) and secondly the examples set by successful partnerships, and the owners hearing of these.

Motivation to consider water services franchising partnerships would not necessarily only be based on the need for the owners to comply with standards (such as water reliability and quality standards) or about infrastructure asset management. It could also be based on the owners perceiving the attractiveness of the returns from improving operation and maintenance of water services infrastructure. These returns can be substantial – returns, that is, measured in terms of for example water loss reduction, improved wastewater treatment works effluent quality, and more reliable water supply.

The above are of course simply reasons to practice improved operation and maintenance. Water services franchising partnerships would need to be demonstrated as a powerful means of achieving this better operation and maintenance, and/or doing it on a better value for money basis from the infrastructure owner's point of view. The access that franchising gives to quality management, specialist technical advice, and so on – as spelled out in previous chapters – should be a powerful selling tool.

The risk to franchising is that one or more franchising partnerships fail to deliver these advantages. This risk can be reduced by careful selection of site, of franchisor, of franchisees and – it has to be said – of the infrastructure owner and client. The importance of knowledgeable clients, and their own competence in respect of essentials such as being able to pay their contractors in full and on time, must be emphasised. For example, if payment to microenterprises is delayed even for days, never mind weeks, they could be severely harmed or even put out of business – their financial reserves, if any, are invariably minimal.

As noted in Chapter 8, whereas a WSA may require contractual recourse not only to the franchisee, but also to the franchisor, the franchisor could be a co-signatory to the contract or a guarantor of the performance of the franchisee. The WSA may require contractual assurance that the franchisee will be supported by strong management, and that the franchisor is able to make alternative arrangements that will ensure continuity of service should the franchisee fail to meet its contractual obligations to the WSA. Especially this could be necessary if the franchisor's expertise or track record is a significant reason for contracting with the franchisee, and the franchisee is a largely unknown quantity.

Furthermore, the franchisor could be of direct assistance to the franchisee in the event that the client infrastructure owner does not fulfil its contractual obligations. For example, in the event of delayed payment mentioned above, the franchisor would certainly be in a much better position to persuade the client to fulfil those obligations than an entrepreneur, apart from other disadvantages, possibly located some considerable distance from the owner's offices, would be.

Whereas a business based on a single element of the water services delivery value chain might not be viable, a franchisee might be able to build a viable business by offering several water-related operation and maintenance services, thereby achieving dual objectives, viz.:

- economy of scale; and
- lessening dependence on one or a limited number of clients.

In order to still further improve the size and especially the reliability of their revenue stream, it would invariably appear to be prudent for franchisors and franchisees to undertake forms of activity additional to operation and maintenance – for example construction work, and/or materials supply.

Finally: water services franchising partnerships will of course be limited to the extent that suitable franchisors are willing and available, and suitable local entrepreneurs are willing and able to take up water services franchise opportunities. Also that franchising proves to be a viable business for franchisor and franchisee alike, and that service to customers meets the specification in the franchise contract with the WSA or WSP.

12. Resources

A search for documentation on non-water services franchising, even if the search is undermined to South Africa, will find much in the way of books, specialist magazines, articles in newspapers and general business magazines, and online material. (Of the books, the most useful for current purposes are Illetschko, 2005 and FASA 2005.) There are several consultants in the field, offering advice on and assistance with a range of services, including concept development, assessment of franchisors (for potential franchisees), assessment of potential franchisees (for franchisors), introductions between franchisors and potential franchisees, site selection, business planning, access to finance, training and BEE opportunities.⁸ There is a large body of legal case law. Seminars on one or other aspect of franchising are frequently held, and there is even an annual exhibition of franchising.

These are of use to those interested in being water services franchising partners in the form of either franchisors or franchisees, or to water services infrastructure owners. But only up to a point. None of them has hitherto shown much interest in water services, or to anything in the line of what the franchise industry refers to as "social franchising". (Or, in the case of publications, makes any reference to water services or social franchising.⁹)

⁸ Apart from companies, such as finance houses and legal firms, that offer franchising-related services as one of their many areas of expertise, there are specialist franchising professional services providers such as Business Partners, Arrow Franchising, Franchise Directions and Franchising Plus – among others. Contact information on these and other firms offering services can be obtained from FASA.

⁹ Publications are usually written with one or other audience in mind. For example the FASA directory is aimed at entrepreneurs looking to become franchisees of established franchises – the subtitle "10 steps to acquiring a successful franchise" makes this clear (FASA 2004). Illetschko is aimed at the same audience – it is titled "Become a franchisee". The FASA manual, on the other hand, "focuses firmly on the needs of franchisors" (FASA 2005 page 30).

Nonetheless, it is these principles, a common theme in the publications and in advice from franchising consultants, that are extremely valuable to all interested in franchising – water services franchising partnerships included. These basic principles, to be considered when franchising the provision of any kind of service (and franchising of water services operation and maintenance would be no exception), are referred to extensively in the current document. They include:

- The need for hands-on experience.
- That franchisors must run "branches" of their business as close as possible in product, environment, customer and all other necessary aspects, to that which a franchisee would need to face. Then the franchisor must iron out the problems – and only thereafter contemplate franchising the undertaking.
- The need for contract agreements to be tailored to the franchising – and that the franchising agreements can only be developed after the basic components of the franchise package have been developed, tested and documented.

Virtually all the information on water services franchising partnerships in South Africa that is in the public domain can be found in the earlier WRC report (Wall, 2005) and in the WRC reports compiled during the course of its research in collaboration with CSIR. They contain a mine of information. The case study of a hypothetical situation will be of particular value to those interested in wishing to explore the business opportunities and/or service delivery opportunities in water services franchising partnerships.

However the reports do not contain simple answers to possible questions such as "I think I have an entrepreneurial bent (or I already own or run a SMME) – how can I become a water services franchisee?", or "I am an owner of water services infrastructure – how can I find out if (i) operation and maintenance of any of it is franchisable, and (ii) if contracting with franchisee partners will bring the advantages that I am looking for?". For good reason – there are no simple answers to these questions, and the first part of any answering process would in any case be "it depends". "It depends", for example, what state is the infrastructure in, what skills are required, what budgets are available to operate and maintain this infrastructure, who is running it now – and many other questions.

As noted, even in respect of conventional franchising, the manuals, consultants and the like go to great lengths to make it clear where their advice is non-specific, and that specialist advice, specific to the possibilities in mind, must be consulted thereafter.

The reason for mentioning this is to point out that these books are written in a context that assumes acceptance of the franchising concept and sophistication in its implementation. I.e. either that the franchising modelling has been done, the model has been tried and tested in practice, and it is working – or that there is an entrepreneur who has an established business and wishes to consider franchising it. In contrast, the concept of water services franchising partnerships is little known, let alone have water services franchising partnerships become a tried and tested – and accepted – alternative to WSAs' in-house operation and maintenance.

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